

BEFORE
THE PUBLIC SERVICE COMMISSION OF
SOUTH CAROLINA
DOCKET NO. 96-160-S - ORDER NO. 97-517
JUNE 17, 1997

✓

IN RE: Application of Midlands Utility, Inc.) ORDER
for Approval of an Increase in Rates) APPROVING
and Charges for Sewer Service for its) INCREASE IN
Customers in Richland, Lexington,) RATES AND CHARGES
Fairfield, and Orangeburg Counties.)

I.
INTRODUCTION

This matter comes before the Public Service Commission of South Carolina (the "Commission") on the Application of Midlands Utility, Inc. ("Midlands" or the "Company") filed December 17, 1996. In its Application, Midlands requested approval of a new schedule of rates and charges for water and wastewater ("sewer") service provided to its customers in its service area in South Carolina. The Application was filed pursuant to S.C. Code Ann. §58-5-240 (Supp. 1996) and 26 S.C. Regs. 103-821 (1976).

By letter dated January 9, 1997, the Commission's Executive Director instructed Midlands to publish a prepared Notice of Filing, once, in newspapers of general circulation in the area affected by the Application. The Executive Director also directed the Company to furnish, by U.S. Mail, a copy of the Notice of Filing to each customer. The Company complied with the instructions of the Executive Director and supplied an Affidavit

of Publication and a Certificate of Service as proof of compliance. The Notice of Filing indicated the nature of the Company's Application and advised all interested persons desiring participation in the scheduled proceeding of the manner and time in which to file the appropriate pleadings for participation in the proceeding. Petitions to Intervene were filed by the Consumer Advocate for the State of South Carolina (the "Consumer Advocate") and Joseph L. Crump.

The Company's presently authorized rates and charges were approved by Commission Order No. 92-84 dated February 28, 1992, in Docket No. 90-528-S; by Commission Order No. 92-244 dated April 10, 1992, in Docket No. 91-568-S; and by Commission Order No. 94-367 dated April 22, 1994, in Docket No. 94-235-S. According to the Company's Application, as depicted in Second Revised Exhibit 4 to the Application, the requested rates would increase sewer service revenue by \$188,749.

The Commission Staff made on-site investigations of the Company's facilities, audited the Company's books and records, and gathered other detailed information concerning the Company's operations. The Consumer Advocate also conducted discovery in the rate filing of Midlands.

On May 13, 1997, at 2:30 p.m., the Commission convened a public hearing in the Commission's hearing room at 111 Doctors Circle in Columbia, South Carolina. Pursuant to S.C. Code Ann. §58-3-95 (Supp. 1996), a panel of three (3) Commission members was designated to hear and rule on this matter. The panel was

composed of Commissioner C. Dukes Scott, presiding; Commissioner Cecil A. Bowers; and Commissioner Philip T. Bradley. Frank R. Ellerbe, III, Esquire and Bonnie D. Shealy, Esquire represented the Company; Elliott F. Elam, Jr., Esquire represented the Consumer Advocate; and Florence P. Belser, Staff Counsel, represented the Staff. The Intervenor Joseph L. Crump did not appear.

The Company presented the testimony of Keith G. Parnell, Vice President and Operations Manager of Midlands; Stan Bennett, C.P.A.; and Anastasia Hunter-Shaw of the South Carolina Department of Health and Environmental ("DHEC"). The Consumer Advocate presented the testimony of Philip E. Miller of Riverbend Consulting. The Commission Staff presented the testimony of Bruce Hulton of the Commission's Accounting Department, and Charles A. Creech of the Commission's Utilities Department, to report Staff's findings and recommendations. One public witness, Eleese H. Benton, appeared and offered testimony.

II. FINDINGS OF FACT

Based upon the Application, the testimony and exhibits received into evidence at the hearing, and the entire record of these proceedings, the Commission now makes the following findings of fact:

1. Midlands is a sewer utility providing sewer service in its service areas within South Carolina, and its operations in South Carolina are subject to the jurisdiction of the Commission,

pursuant to S.C. Code Ann. §58-5-10 et seq. (1976), as amended.

2. The appropriate test period for the purposes of this proceeding is the twelve month period ending June 30, 1996.

3. According to the Company's Application, the Company is seeking an increase of its rates and charges for sewer operations of \$188,749.

4. The appropriate operating revenues, as adjusted herein, for the Company for the test year under its presently approved rates are \$633,639.

5. The appropriate, as adjusted, operating expenses for the Company's operations for the test year under its present rates are \$634,796.

6. The Company's net operating income and total income for return for the test year, after adjustments approved herein, is calculated to be (\$1,157).

7. The Commission will use the operating margin as a guide in determining the lawfulness of the Company's proposed rates and the fixing of just and reasonable rates.

8. A fair operating margin that the Company should have the opportunity to earn is 12.46% which is produced by the appropriate level of revenues and expenses found reasonable and approved herein.

9. The rate designs and rate schedules approved by the Commission as described herein are appropriate and should be adopted.

10. The rates and charges depicted in Appendix A, attached

hereto and incorporated by reference, are approved and effective for service rendered on and after the date of this Order.

III.
EVIDENCE AND CONCLUSIONS

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 1.

The evidence supporting this finding concerning the Company's business and legal status is contained in the Company's Application and in prior Commission Orders in the docket files of which the Commission takes judicial notice. The Company is a sewer utility under S.C. Code Ann. §58-5-10 and is providing sewer service in its approved service area in Fairfield, Lexington, Orangeburg, and Richland Counties, South Carolina. The Company's operations are subject to the jurisdiction of this Commission. This finding of fact is essentially informational, procedural, and jurisdictional in nature, and the matters which it involves are uncontested.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 2.

The evidence for this finding concerning the appropriate test period is contained in the Company's Application and in the testimony and exhibits of the Company witnesses, the witness for the Consumer Advocate, and the Staff's witnesses. The Company proposed in its Application that the appropriate test year be which to consider the requested rate increase was the twelve month period ending June 30, 1996, and based the filing on that time period. Relying on the Company's proposed test year, the Staff and the witness for the Consumer Advocate utilized the same test

period for their accounting and pro forma adjustments.

A fundamental principle of the ratemaking process is the establishment of a historical test year period. While the Commission considers a utility's proposed rate increase based upon occurrences within the test year, the Commission will also consider adjustments for any known and measurable out-of-test year changes in expenses, revenues, and investments, and will also consider adjustments for any unusual situations which occurred in the test year. See, Parker v. South Carolina Public Service Commission, 280 S.C. 310, 313 S.E. 2d 290 (1984), citing City of Pittsburgh v. Pennsylvania Public Utility Commission, 187 P.A. Super. 341, 144 A.2d 648 (1958); Southern Bell v. The Public Service Commission, 270 S.C. 590, 244 S.E.2d 278 (1978). Based on the record, the Commission finds the twelve month period ending June 30, 1996, to be the reasonable and appropriate period in which to make its ratemaking determinations herein.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 3.

The evidence for this finding concerning the requested amount of increase is found in the Company's Application and in the Staff's Report - Utilities Department, Exhibit B (Hearing Exhibit No. 5). According to the Company's Application and its Second Revised Exhibit 4, the proposed rates will increase sewer revenues by \$188,749. Hearing Exhibit No. 6, which is the portion of the Staff Report submitted by the Utilities Department, contains Exhibit B which also shows the requested rates will increase sewer revenues by \$188,749. Staff calculated the proposed revenues

using actual billing units.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 4.

The Company's Second Revised Exhibit 4 to the Application delineated as adjusted revenues in the amount of \$667,827 for the test year. Staff proposed adjustments to revenues which resulted in adjusted test year revenues of \$632,377.

The Commission adopts the following adjustments to revenues:

Staff proposed an adjustment of (\$31,044) to remove tap fees from operating revenues. Both the Consumer Advocate and the Company included revenues from tap fees in pro forma operating revenues. Staff did not exclude tap expenses from cost of service. The Consumer Advocate contends that it is not proper to exclude tap revenues if tap expenses are not also excluded. The Commission concludes that tap fees are items which should be capitalized and should be excluded from operating revenues. Therefore, the Commission adopts Staff's adjustment and will address the Consumer Advocate's contention that tap expenses should also be excluded in the discussion concerning Finding of Fact No. 5.

Staff and the Company proposed an adjustment of \$7,972 to per book revenues to account for amortization of present rates. Staff and the Company also proposed an adjustment of (\$2,533) to remove Interest Income from Operating Income. The Commission finds Staff's adjustments appropriate and hereby adopts Staff's adjustments.

At the hearing, Mrs. Elease H. Benton, the public witness,

alleged that Midlands had not collected from all the residences in her subdivision. In response to Mrs. Benton's testimony, Mr. Parnell admitted that Midlands had identified five (5) houses that had tapped into the system without Midlands' knowledge and that Midlands had notified these five (5) persons that payment for service would be required.

The Commission finds that the revenues associated with these five (5) additional customers should be included in test year revenues. In its post-hearing brief, Staff calculated that five additional customers during the test year would increase test year operating revenues by \$1,262. The Commission adopts this amount as the appropriate adjustment to test year revenues.

The total offset of the adjustments adopted herein is to reduce the Company's book operating revenues by (\$24,343) which results in adjusted operating revenues of \$633,639.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 5.

For the reasons set forth below, the Commission approves the following accounting and pro forma adjustments to test year expenses. All recommendations and adjustments proposed by the parties that are not specifically discussed herein or that are inconsistent with the accounting and pro forma adjustments proposed by the Commission Staff are denied.

(a) The Staff removed tap fee revenues from operating revenues, and the Commission accepted Staff's adjustment to revenues above. The Consumer Advocate takes the position in his brief that "both tap revenues and tap expenses should be excluded,

or in the alternative they both should be included." (Brief of the Consumer Advocate, p. 3). The Consumer Advocate also proposes inclusion of both tap fee revenues and tap expenses as the Consumer Advocate suggests that the record does not contain any data regarding the expenses associated with installing taps. (Brief of the Consumer Advocate, p. 3).

The Commission believes that the expenses associated with installing the taps should be excluded from cost of service. The Commission has removed tap fee revenues from operating revenues as tap fees are items which properly should be capitalized. As an item that should be capitalized, the Commission finds it appropriate to remove from operating expenses the expenses associated with making the taps. The Company's tap fees were previously approved by Commission Order and presumably reflect the cost of making the tap. Therefore, the Commission believes and concludes that expenses associated with making the taps should be removed from operating expenses in an amount equal to the tap fees collected. The amount of this adjustment shall be (\$31,044) which reflects the amount of tap fee revenues collected during the test year.

(b) The Company proposed to increase its test year treatment expense by \$115,830. The Company's adjustment was based on the following three elements:

1. The City of Cayce increased the rates it charges the Company for treatment expense by raising the cost by 150%. This increase in the cost of treatment was permitted pursuant to the

Order of Confirmation of the United States Bankruptcy Court entered February 1, 1995. (See, In re: Midlands Utility, Inc., Case Number 94-72521.) The Company showed a projected annual cost of \$111,360, which included a 9.42% customer volume increase.

2. Treatment expense payable to Carolina Water Service, Inc. ("CWS") for treatment of sewerage generated in the Vanarsdale Subdivision. The treatment contract between CWS and Midlands was previously approved by the Commission. The Company projects yearly treatment costs of \$54,912 under the contract with CWS for treatment of the sewerage from the Vanarsdale Subdivision.

3. Treatment expense payable to the City of Orangeburg for treatment of wastewater from the Northwood Estates Subdivision in Orangeburg. At the time of the hearing, the treatment contract between Midlands and the City of Orangeburg had been approved by the Commission. The Company projects yearly treatment costs of \$15,355.

The Staff proposed an adjustment to treatment expense of \$100,475. Staff's adjustment included costs of treatment pursuant to the Commission approved contracts with the City of Cayce and with CWS. However, Staff did not include the contract with the City of Orangeburg because that contract was neither finalized nor approved as of the date of Staff's audit.

The Consumer Advocate proposed two modifications to the Company's proposed adjustment. The Consumer Advocate proposed removing a projected increase in customer volume of 9.42% from the City of Cayce treatment expense and also proposed that the costs

associated with treatment provided under the City of Orangeburg contract be excluded. The Consumer Advocate asserts that the projected 9.42% increase in volume with the City of Cayce is not known and measurable. Further, the Consumer Advocate asserts that the costs associated with treatment to be provided by the City of Orangeburg are premature as the contract had only been approved the day of the hearing and that it will be approximately three months before the City of Orangeburg will begin treating the wastewater from the Northwood Estates Subdivision.

Upon consideration of this matter, the Commission concludes that the Company's proposed adjustment should be modified to remove the 9.42% customer volume increase, which quantified is (\$9,587), from the City of Cayce treatment expense. The Commission believes that the Company should be allowed to recover in rates the costs of treatment provided under Commission approved contracts. However, the Commission agrees with the Consumer Advocate that the 9.42% customer volume increase is not known and measurable and should therefore be excluded. While the City of Orangeburg contract was only approved the day of the hearing, testimony of record reveals that the connection with the City of Orangeburg needs to be made as soon as possible and that construction on the connection will begin as soon as construction permits are issued. Therefore, the Commission finds the treatment expense associated with the City of Orangeburg contract appropriate. The Commission finds the Company's adjustment, excluding the 9.42% increase in the City of Cayce treatment

component, reasonable in light of the evidence and concludes that an adjustment of \$106,243 will allow the Company to properly recover the costs for treatment of sewerage provided pursuant to its contracts.

(c) The Commission concludes that Operation and Maintenance (O & M) expense of (\$1,000) associated with the Orangeburg lagoon included in the test year should be excluded. During the hearing, Mr. Parnell testified that Midlands incurs approximately \$6,000 in operational costs with the operation of the Orangeburg (Northwoods) treatment lagoon. Mr. Parnell testified that of that \$6,000, approximately \$1,000 is for lab testing, chemicals, and grass mowing that will not be recurring, while approximately \$5,000 is for the salary of the employee who monitored the lagoon. Mr. Parnell further testified that the employee's salary will continue as that employee will remain with the Company. As the record reveals that (\$1,000) in O & M expenses associated with the Orangeburg lagoon will not be recurring once treatment by the City of Orangeburg begins and as the Commission has approved herein the treatment costs associated with treatment by the City of Orangeburg, the Commission concludes that (\$1,000) should be removed from O & M expenses.

(d) At the hearing, the Company updated rate case expenses to show a total of \$13,772. The Company requested inclusion of the updated rate case expenses amortized over three (3) years. The Staff recommended a three (3) year amortization of rate case expenses, while the Consumer Advocate recommended amortization

over five (5) years. As the basis for its proposed five year amortization, the Consumer Advocate states in his brief that the Company did not incur any rate case costs during the period of 1992 through 1996.

Upon consideration of this issue, the Commission finds a three year amortization of the Company's updated rate case expenses to be reasonable. The Commission believes that a three year amortization period is a reasonable and sufficient time for the Company to recover these expenses. Therefore, the Commission adopts the Company's proposed adjustment of \$13,772 amortized over a three (3) year period.

(e) The Company proposed an adjustment of \$19,350 to Depreciation and Amortization expense. This adjustment reflects the expense associated with the CWS tap fee of \$83,000 (for the treatment of the Vanarsdale Subdivision) and the City of Orangeburg tap fee of \$13,750 (for the Northwoods Estates subdivision) amortized over five (5) years.

Staff proposed an adjustment to Depreciation and Amortization expense of \$2,075. This adjustment was to adjust the amortization of tap fees to Carolina Water Service ("CWS") associated connecting with CWS for treatment of wastewater from Midlands' Vanarsdale subdivision. Staff proposed an amortization period of forty (40) years, which Staff calculated to be the life of the line. Staff did not include any costs associated with the contract with the City of Orangeburg in Staff's adjustment.

The Consumer Advocate proposed a sixteen (16) year

amortization period for the CWS connection. The Consumer Advocate's reasoning was that had Midlands upgraded the Vanarsdale treatment facility then Midlands would have depreciated the upgrading over the expected service life of the treatment facility adjustment. Thus the Consumer Advocate asserts that the same treatment should be given to the tap (impact) fee payable to CWS. At the hearing the witness for the Consumer Advocate stated that he would support the amortization period proposed by Staff. Further, the Consumer Advocate did not include the costs of the tap with the City of Orangeburg as the Consumer Advocate asserts that inclusion of that cost is premature.

Upon consideration of this matter, the Commission concludes that the Company's adjustment should be adopted. The length of the note under which Midlands has to pay CWS for the tap (impact) fee is five years. Further, Midlands requested at the hearing that the Commission take judicial notice that the CWS I-20 treatment facility is considered a temporary treatment facility that will be closed pursuant to the Clean Water Act's Section 208 area-wide waste treatment management plan. Midlands therefore asserts that since the CWS facility is not a permanent treatment facility then a forty (40) or sixteen (16) year amortization would not be appropriate. The Commission agrees that a five (5) year amortization period is reasonable and appropriate under the circumstances of the instant case. Further, the Commission concludes that the tap fee payable to the City of Orangeburg should be included in the instant case and that the City of

Orangeburg tap fee should be afforded the same accounting treatment as the tap fee with CWS. Therefore, the Commission approves the Company's adjustment of \$19,350.

(f) Staff proposed an adjustment to annualize the salary for Midlands President to reflect a salary of \$800 per week. This adjustment reduced operating and maintenance ("O & M") expense by (\$96,156). Midlands proposed the same adjustment. The Consumer Advocate proposed that the salary for the Company's President for ratemaking purposes be set at \$32,240 which the Consumer Advocate asserts reflects the President's salary as of December 31, 1996.

The Commission accepts Staff adjustment on the proper level of the salary for the Company President. The Staff's, and the Company's, adjustment reflects a salary of \$800 per week. The witness for the Consumer Advocate indicated on cross examination that an \$800 per week salary was not unreasonable. The Commission finds that a salary of \$800 per week for the Company President is reasonable and approves Staff's adjustment of (\$96,156).

(g) Staff proposed an adjustment of \$519 to O & M Expense to adjust Collection Salaries and Wages to reflect year-end salaries. Midlands proposed the same adjustment. Staff also proposed to adjust General Expenses by (\$1,251) to adjust Administrative Salaries to reflect end of year rates. Midlands proposed the same adjustment. The adjustments proposed by Staff and by the Company include a 15% salary increase granted to Midlands employees. The Consumer Advocate took exception to the 15% wage increase and proposed a 7.5% wage increase for ratemaking purposes.

The record reveals that Midlands granted a 15% wage increase to its employees at the same time that a similar increase was granted to employees of Bush River Utilities, Inc. and Development Service, Inc., which are sister companies of Midlands. The record further reveals that prior to the 15% wage increase, employee salaries had not been increased for five years.

Upon examination of this matter, the Commission concludes that Staff's adjustment, which includes the 15% wage increase, should be approved. The salary increase has been given to the employees and is not something that is expected to occur in the future. The increase is known and measurable, and in light of the length of time since salaries were increased, the Commission believes and finds that the wage increase is reasonable. Therefore, the Commission adopts Staff's and the Company's adjustments of \$519 to O & M Expense to adjust Collection Salaries and Wages to reflect year-end salaries and of (\$1,251) to General Expenses to adjust Administrative Salaries to reflect end of year rates.

(h) Staff proposed an adjustment to O & M Expense of \$6,643 to reflect an increase in the cost of chemicals. Staff's adjustment was based on the amounts shown in the engineering report. The Company proposed an adjustment of \$5,008 increased cost of chemicals, but the Company's adjustment was based on an earlier study. The Consumer Advocate witness reviewed the Staff's chemical expense adjustment and recommended that the Commission adopt the Staff's proposed chemical expense adjustment.

The Commission concludes that Staff's chemical expense adjustment reflects the proper chemical expense. Therefore, the Commission adopts the Staff's chemical expense adjustment of \$6,643 as reasonable and appropriate.

(i) Staff proposed adjustments of (\$767) to O & M Expenses and (\$3,326) to General Expense to eliminate non-allowable items from expenses. These non-allowables included flowers, non-company automobile insurance, and non-company automobile repairs. The Company did not remove any non-allowable items. The Consumer Advocate agreed with the elimination of insurance expense associated with automobiles assigned to the spouse of the Company President and to Ken Parnell, a part-time employee of the Company, and the Consumer Advocate further recommended an adjustment of (\$2,601) to remove the costs of health insurance for the spouse of the Company President.

Upon consideration of this adjustment, the Commission finds and concludes that Staff's adjustment is appropriate and hereby adopts the Staff adjustment to eliminate non-allowable items.

(j) Staff eliminated (\$3,260) from General Expense to remove costs associated with an item that should have been capitalized rather than expensed. The Commission accepts Staff's adjustment as reasonable as the cost of capitalized items should not be included in expenses.

(k) Both the Staff and the Company proposed to annualize Depreciation Expense. Using standard service lives, Staff proposed an adjustment of \$8,233 and restated depreciation. At

the hearing, Midlands accepted and agreed with Staff's adjustment. The Consumer Advocate did not propose a corresponding adjustment.

The Commission hereby accepts the Staff's adjustment as appropriate and reasonable.

(l) Staff proposed an adjustment of (\$1,270) to adjust payroll taxes for the effect of annualized payroll. Staff used a rate of 7.65%. Midlands used a rate of 8% and proposed an adjustment of (\$694). The Consumer Advocate accepted the 8% relationship between payroll taxes and salaries and wages and proposed an adjustment of (\$3,275).

The Commission concludes that Staff's adjustment should be accepted. The 7.65% is the correct rate for social security used by the Federal Government. Therefore, the Commission concludes that the adjustment based on the rate actually used should be adopted.

(m) Staff proposed an adjustment of \$3,192 to annualize interest on Customer Deposits. Midlands nor the Consumer Advocate made a comparable adjustment.

The Commission adopts Staff's adjustment. The Commission concludes that this adjustment is appropriate as it recognizes the interest expense associated with the customer deposit balance at year end.

(n) The Staff proposed an adjustment of (\$1,148) for interest synchronization. The Consumer Advocate stated in his brief that he agrees with the Staff that the interest expense should be synchronized with the adjusted rate base. The Company

did not propose an adjustment for interest synchronization.

The Commission adopts Staff's adjustment. Staff shows the operating margin for "Per Book Operations" used the interest as shown in the Company's Application. Staff then used \$23,078 for interest "As Adjusted" and "After the Proposed Increase." Staff states that this amount represents imputed interest calculated when synchronizing interest to rate base. Staff also used a 50-50 equity to debt ratio. The Commission finds Staff's adjustment reasonable and hereby adopts Staff's adjustment.

(o) Staff proposed an adjustment to properly reflect income taxes based on taxable income. Staff's adjustment of (\$10,697) reflects a true-up of income taxes to properly reflect no taxable income. Neither the Company nor the Consumer Advocate made this adjustment. The Commission finds Staff's adjustment to true-up income taxes is appropriate and adopts Staff's adjustment.

(p) Staff and the Consumer Advocate proposed an adjustment for customer growth. The customer growth adjustment is made to recognize the offset of the growth in customers. In calculating customer growth, Staff used a formula method based on growth in customer totals applied to all income and expenses. The Consumer Advocate also used a formula approach but eliminated some expenses which the Consumer Advocate states are not affected by growth in customers.

Upon consideration of this issue, the Commission concludes and determines that Staff's adjustment is appropriate and reasonable as the Commission believes that Staff's adjustment

gives a fair and reasonable projection of customer growth. The Commission does not find the method utilized by the Consumer Advocate to be persuasive. Therefore, the Commission adopts the customer growth adjustment proposed by Staff.

The total effect of the above approved adjustments to expenses reduces per book operating expenses by (\$1,148) and results in as adjusted total operating expenses of \$634,796.

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NO. 6.

Based on the accounting and pro forma adjustments herein approved, the Company's appropriate total income for return for the test year for the computation of an appropriate operating margin is (\$1,157). The calculation of total income for return is shown in Table A:

TABLE A

TOTAL INCOME FOR RETURN - AS ADJUSTED

Operating Revenues	\$ 633,639
Operating Expenses	634,796
Net Operating Income	\$ (1,157)
Customer Growth	0
Total (Net) Income for Return	<u>\$ (1,157)</u>

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NOS. 7 AND 8.

Under the guidelines established in the decisions of Bluefield Water Works and Improvement Co. v. Public Service Commission of West Virginia, 262 U.S. 679 (1923), and Federal Power Commission v. Hope Natural Gas, 320 U.S. 591 (1944), this Commission does not ensure through regulation that a utility will

produce net revenues. As the United States Supreme Court noted in the Hope Natural Gas decision, supra, the utility "has no constitutional rights to profits such as are realized or anticipated in highly profitable enterprises or speculative ventures." However, employing fair and enlightened judgment and giving consideration to all relevant facts, the Commission should establish rates which will produce revenues "sufficient to assure confidence in the financial soundness of the utility and ... that are adequate under efficient and economical management, to maintain and support its credit and enable it to raise the money necessary for the proper discharge of its public duties." Bluefield, supra, at 692-693.

Neither S.C. Code Ann. §58-5-240 (Supp. 1996) nor any other statute prescribes a particular method to be utilized by the Commission to determine the lawfulness of the rates of a public utility. For ratemaking purposes, this Commission examines the relationships between expenses, revenues, and investment in a historic test period because such examination provides a constant and reliable factor upon which calculation can be made to formulate the basis for determining just and reasonable rates. This method was recognized and approved by the South Carolina Supreme Court for ratemaking purposes involving utilities in Southern Bell Telephone and Telegraph Co. v. The Public Service Commission of S.C., 270 S.C. 590, 244 S.E. 2d 278 (1978).

For water and sewer utilities, where the utility's rate base has been substantially reduced by customer donations, tap fees,

and contributions in aid of construction or where the utility may not have a rate base, the Commission may decide to use the "operating margin" as a guide in determining just and reasonable rates, instead of examining the utility's return on its rate base. The operating margin is determined by dividing total income for return (or net operating income) less interest expense by the operating revenues of the utility.

The Commission believes that its use of the operating margin has resulted in fair rates to both the utility and the ratepayer and finds and concludes that the operating margin is the appropriate method by which to set rates in the instant case. This method was recognized as an acceptable guide for ratemaking purposes in Patton v. South Carolina Public Service Commission, 280 S.C. 288, 312 S.E. 2d 257 (1984). Therefore, the Commission will use the operating margin as a guide in determining the lawfulness of the Company's proposed rates and the fixing of just and reasonable rates.

The following Table indicates the Company's gross revenues for the test year under the presently approved rate schedules; the Company's operating expenses for the test year; and the operating margin under the presently approved schedules for the test year:

TABLE B

OPERATING MARGIN - AS ADJUSTED

Operating Revenues	\$ 633,639
Operating Expenses	634,796
Net Operating Income	\$ (1,157)
Customer Growth	0
Total (Net) Income for Return	\$ (1,157)
Operating Margin (Before Increase) (Less interest of \$23,078)	<u>(3.82%)</u>

The Commission is mindful of those standards delineated in the Bluefield decision, supra, and of the balance between the respective interests of the Company and of the consumer. The Commission has considered the spectrum of relevant factors in this proceeding, including among others: the revenue requirements for the Company, the price for which the Company's service is rendered as well as the proposed price, the quality of that service, and the effect of the proposed price upon the consumer.

The three fundamental criteria of a sound rate structure have been characterized as follows:

...(a) the revenue-requirement or financial-need objective, which takes the form of a fair-return standard with respect to private utility companies; (b) the fair-cost apportionment objective which invokes the principle that the burden of meeting total revenue requirements must be distributed fairly among the beneficiaries of the service; and (c) the optimum-use or consumer rationing under which the rates are designed to discourage the wasteful use of public utility services while promoting all use that is economically justified in view of the relationships between costs incurred and benefits received.

Bonbright, Principles of Public Utility Rates (1961), p. 292.

The Commission has considered the proposed increase presented by the Company in light of the various standards to be observed and the interests represented before the Commission. The Commission has also considered the impact of the proposed increase on the ratepayers of the Company. The Commission must balance the interests of the Company -- the opportunity to make a profit or earn a return on its investment, while providing adequate water service -- with the competing interests of the ratepayers -- to receive adequate service at a fair and reasonable rate.

In light of those factors as previously discussed, and based upon the record in the instant proceeding, the Commission concludes that a fair operating margin that the Company should have an opportunity to earn is 12.46% which will require annual operating revenues of \$800,139. The following table reflects an operating margin of 12.46%:

TABLE C

OPERATING MARGIN - AS APPROVED

Operating Revenues	\$ 800,139
Operating Expenses	678,924
Net Operating Income	\$ 121,215
Customer Growth	1,555
Total (Net) Income for Return	\$ 122,770
Operating Margin (After Increase) (Less interest of \$23,078)	<u>12.46%</u>

In developing rates to give the Company the required operating revenues so that it will have the opportunity to achieve a 12.46% operating margin, the Commission has carefully considered

the needs of the Company's customers with the needs of the Company. The rates designed herein, and which appear in Appendix A attached hereto, consider the quality of service provided by the Company to its customers, the need for the continuance of the provision of adequate service, and the need of the Company to meet its financial obligations, as well as the impact of the increase on those customers receiving service. The rates and charges approved herein are designed in such a manner as to produce and distribute the necessary revenues to provide the Company with the opportunity to earn the approved operating margin.

IT IS THEREFORE ORDERED THAT:

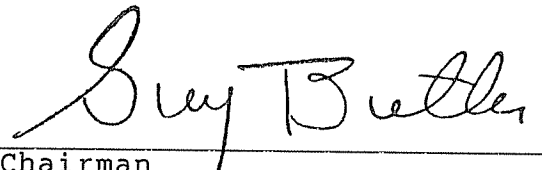
1. The proposed schedule of rates and charges as filed in the Company's Application is found to be unreasonable and is hereby denied.

2. The schedule of rates and charges attached hereto as Appendix A is hereby approved for service rendered on or after the date of this Order. The schedule is deemed filed with the Commission pursuant to S.C. Code Ann. §58-5-240 (Supp. 1995).

3. The Company shall maintain its books and records in accordance with the NARUC Uniform System of Accounts, as adopted by this Commission.

4. This Order shall remain in full force and effect until further Order of this Commission.

BY ORDER OF THE COMMISSION:


Chairman

ATTEST:


Deputy Executive Director

(SEAL)

APPENDIX A

MIDLANDS UTILITY, INC.
P. O. BOX 887
LEXINGTON, SC 29072
(803) 359-4803

Docket No. 96-160-S
Order No. 97-517
June 17, 1997

PROPOSED RATES AND CHARGES

<u>Residential</u>		
Permanent Base	-	\$ 26.70
Apartment	-	\$ 26.70
Mobile Base	-	\$ 20.30
<u>Commercial</u>		
Convenience	-	\$ 26.70
Other	-	\$ 26.70 per SFE
<u>Tap Fees</u>		
Residential	-	\$250.00 per SFE
Commercial	-	\$250.00 per SFE
<u>Plant Expansion and Modification</u>		
<u>Fees for Customer's Sewer Not</u>		
<u>Treated by City of Cayce</u>		
Residential	-	\$250.00 per SFE
Commercial	-	\$250.00 per SFE
<u>Other Charges</u>		
New Customer Set-Up	-	\$ 25.00
Disconnect Notice	-	\$ 4.00